

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

In the Matter of the Application of Southern California Gas Company Regarding Year Seven (2000-2001) Under Its Experimental Gas Cost Incentive Mechanism and Related Gas Supply Matters. (U 904 G)

Application 01-06-027  
(Filed June 15, 2001)

**SCOPING MEMO AND RULING OF THE ASSIGNED COMMISSIONER  
AND ADMINISTRATIVE LAW JUDGE REGARDING YEAR SEVEN OF  
THE GAS COST INCENTIVE MECHANISM**

**Summary**

Southern California Gas Company (SoCalGas) filed its Year Seven Gas Cost Incentive Mechanism (GCIM) application on June 15, 2001. A joint protest to the application was filed on July 19, 2001, by Southern California Edison Company (SCE) and the Southern California Generation Coalition (SCGC). The California Industrial Group and the California Manufacturers & Technology Association (CIG/CMTA) also filed a protest to the application.<sup>1</sup> A prehearing conference was held on October 29, 2001 and November 6, 2002 to discuss whether the issues raised by the protestants should be examined in this application or elsewhere, and to determine the procedural schedule for processing this application.

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<sup>1</sup> A response to the application was filed by the Office of Ratepayer Advocates (ORA) on July 19, 2001. SoCalGas filed a reply on July 30, 2001 to the protests and to ORA's response.

This scoping memo determines that the concerns of the protestants will be addressed in the Order Instituting Investigation (“investigation” or “I.”) 02-11-040 into the gas price spikes experienced at the California border in 2000 and 2001. The two remaining issues in this proceeding will be addressed in this proceeding without evidentiary hearings.

## **Background**

The joint protest of SCE and SCGC asserts that the existing GCIM structure creates perverse incentives that allows SoCalGas to conduct its operations in a way that benefits shareholders at the expense of customers, harms noncore customers, and detrimentally impacts the California energy markets. SCE and SCGC also assert that as a result of the GCIM structure, SoCalGas engaged in hub services and future market transactions in Year Seven which had a negative effect on SoCalGas’ customers. SCE and SCGC also contend that “SoCalGas has not been authorized to use its GCIM for Year Seven or any year thereafter,” and therefore, SoCalGas does not have an entitlement to any award for Year Seven. (SCE and SCGC Protest, p. 2.)

The protest of CIG/CMTA asserts that the “existing GCIM mechanism produces unjust and unreasonable results,” and “may provide inappropriate gas procurement incentives that may distort the marketplace.” CIG/CMTA also point out that the “Commission specifically deferred its decision of whether to have a GCIM beyond Year 6.” CIG/CMTA also assert that the “GCIM may have contributed significantly to the problem of disproportionately high California border prices.” (CIG/CMTA Protest, pp. 1-3.)

ORA’s response, as well as the two protests, acknowledged that the issues regarding the GCIM structure, and the shareholder award for Year Seven, were being addressed in Phase II of the Year Six GCIM proceeding (A.00-06-023).

ORA's response also notes that SoCalGas, ORA, and The Utility Reform Network filed a joint motion on July 5, 2001 to adopt a settlement which would resolve all issues in Phase II of A.00-06-023 by implementing modifications to the GCIM, and reducing the shareholder award for Year Seven from \$106 million to \$30.8 million. The settlement was opposed by SCE and SCGC.

At the prehearing conference of October 29, 2001, the assigned Administrative Law Judge (ALJ) indicated that due to the uncertainty of whether the proposed settlement in Phase II of A.00-06-023 would be adopted, that another prehearing conference should be held after the Commission votes on whether to adopt the Phase II settlement. Although the ALJ stated at the October 29, 2001 prehearing conference that a scoping memo would issue after consulting with the assigned Commissioner, no scoping memo for Year Seven was issued until today.

After two days of hearing and briefing, the Phase II Year Six GCIM issues were resolved in D.02-06-023. In that decision, the Commission considered whether the GCIM should be extended, and what type of modifications should be made to the GCIM. One of the issues considered in the hearings was SCE's allegation that the GCIM created perverse incentives. The Commission concluded that the objections that SCE raised in the Phase II hearings were speculative and not supported by the evidence, and that another investigation of the GCIM was not needed. The Commission also approved the settlement agreement that was sponsored by SoCalGas, ORA and TURN, and determined that the GCIM should be continued as modified by the terms of the adopted settlement agreement. D.02-06-023 also directed the Energy Division to prepare an investigation into the gas border price spikes that occurred during the winter of 2000 through spring 2001.

A second prehearing conference was held on November 6, 2002. SCE and SoCalGas filed prehearing conference statements in advance of the prehearing conference. At this prehearing conference, the ALJ noted that the Commission was considering opening an investigation into the spikes in gas border prices at the Commission meeting of November 7, 2002, and that the investigation could possibly be the forum in which SCE's concerns about the GCIM structure could be addressed. On November 21, 2002, the Commission adopted I.02-11-040, which opened an investigation into the following issues, among others:

“2. Did any of the utilities’ affiliates or parent companies play a role in causing the increase in border prices? Did concerns about affiliates or parents’ financial position cause utilities to take actions that may have increased gas costs?

“ ...

“4. Did the utilities’ gas cost incentive mechanisms create perverse incentives to increase or otherwise manipulate natural gas prices at the California border? We shall examine whether SoCalGas’ Year 7 and Year 8 operations under the GCIM, enabled them to exercise market power and/or anticompetitive behavior; If so, should these incentive mechanisms be modified or eliminated to prevent such activity.”

I.02-11-040 also stated that any party “may suggest related issues for the Commission’s consideration” as part of the investigation. (I.02-11-040, p. 8.) A prehearing conference in I.02-11-040 was held on January 9, 2003. In an ALJ ruling dated December 17, 2002 in that investigation, interested persons were allowed to identify any additional substantive issues that were not identified in the investigation that they believe should be included within the scope of that investigation.

At the November 6, 2002 prehearing conference for the Year Seven GCIM application, SCE expressed a willingness to have the concerns it raised in its protest addressed in the investigation. (See A.01-06-027, Nov. 6, 2002 Reporter's Transcript, p. 35.)

### **Scope of Issues**

In D.02-06-023, the Commission resolved the issue of whether the GCIM should be extended for Year Seven and beyond, and also whether the GCIM should be modified. The Commission also declined in D.02-06-023 to consider another investigation of the GCIM.

In I.02-11-040, the Commission opened an investigation into the cause of gas border price spikes from March 2000 through May 2001. The first phase of this investigation will "focus on the Sempra Energy Companies to more fully explore the issues raised in SoCalGas' GCIM proceeding...." (I.02-11-040, p. 9.) I.02-11-040 states that:

"If the investigation reveals that the conduct of respondents contributed to the gas price spikes at the California border during the named period, it may modify or eliminate the respondent's [GCIM], reduce the amount of the shareholder award for the period involved, or order respondents to issue a refund to ratepayers to offset the higher rates paid. If the investigation reveals that statutory laws, or rules or orders of the Commission were violated, the Commission may enter into an adjudicatory phase of this investigation."

Based on the actions taken in D.02-06-023 and I.02-11-040, the issues raised by SCE, SCGC and CIG/CMTA in their protests to this application have either been resolved in D.02-06-023, or will be addressed in I.02-11-040. As a result, there are only two remaining issues that need to be addressed in this proceeding. The first issue is whether the calculation of the shareholder award for Year Seven

under the GCIM, as modified by D.02-06-023, is correct or not. The second issue is whether SoCalGas' acquisition operations during Year Seven were reasonable within the context of the authorized GCIM.

As noted at the November 6, 2002 prehearing conference, the first issue is straightforward, and is derived by examining ORA's Monitoring and Evaluation Report dated November 2, 2001. No one contests the way in which the shareholder award was calculated for Year Seven.

The second issue is also addressed in ORA's November 2, 2001 report. Although SCE, SCGC and CIG/CMTA have raised concerns about the way in which the GCIM is structured, and whether SoCalGas' operations amounted to market power, anticompetitive behavior, or was a cause of the high gas prices experienced in late 2000 through spring 2001, both D.02-06-023 and I.02-11-040 have either addressed those concerns or will provide a forum for addressing those concerns. Consequently, the second issue can be addressed without waiting for I.02-11-040 to be resolved.

The two issues identified in this scoping memo do not require hearings in this proceeding. With regard to the first issue, no one disputes the manner in which SoCalGas' shareholder award has been calculated. On the second issue, the concerns of the protestants regarding the GCIM structure will be addressed in the investigation. No other concerns regarding the second issue have been raised which require a hearing. Accordingly, no evidentiary hearings in this Year Seven proceeding will be held.

This application was preliminary categorized as ratesetting in Resolution ALJ 176-3066 on June 28, 2001. Today's ruling confirms that categorization. Anyone who disagrees with this categorization must file an appeal of the categorization no later than 10 days after the date of this ruling. (See Rule 6.4.)

As a ratesetting proceeding, the ex parte rules contained in Rule 7(c) of the Commission's Rules of Practice and Procedure apply to this proceeding.

The principal hearing officer for this proceeding shall be ALJ Wong.

It is expected that this proceeding will be completed within 18 months from the filing of SoCalGas' application.

### **Schedule**

The following is the schedule that will be followed in this proceeding:

Draft decision issued.	February 28, 2003
Comments and reply comments on draft decision.	In accordance with Rule 77.7.
Decision adopted by Commission.	April 3, 2003

### **IT IS RULED** that:

1. Administrative Law Judge John S. Wong is designated the principal hearing officer for this proceeding.
2. The concerns raised by the protestants to this application will be addressed in Investigation 02-11-040.
3. The remaining issues to be determined in this proceeding are as listed in the body of this ruling.
4. The schedule for this proceeding is as listed in the body of this ruling.

Dated January 16, 2003, at San Francisco, California.

/s/ LORETTA LYNCH

Loretta Lynch  
Assigned Commissioner

/s/ JOHN S. WONG

John S. Wong  
Administrative Law Judge



**CERTIFICATE OF SERVICE**

I certify that I have by mail this day served a true copy of the original attached Scoping Memo and Ruling of the Assigned Commissioner and Administrative Law Judge Regarding Year Seven of the Gas Cost Incentive Mechanism on all parties of record in this proceeding or their attorneys of record.

Dated January 16, 2003, at San Francisco, California.

/s/ FANNIE SID

Fannie Sid

**N O T I C E**

Parties should notify the Process Office, Public Utilities Commission, 505 Van Ness Avenue, Room 2000, San Francisco, CA 94102, of any change of address to insure that they continue to receive documents. You must indicate the proceeding number on the service list on which your name appears.